

E-002/AI-94-378 ORDER APPROVING CONTRACT WITH

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Don Storm
Tom Burton
Marshall Johnson
Cynthia A. Kitlinski
Dee Knaak

Chair
Commissioner
Commissioner
Commissioner
Commissioner

In the Matter of a Petition for Approval of
Power Purchase Agreement Between Northern
States Power Company and Minnesota
Methane, LLC

ISSUE DATE: February 1, 1995

DOCKET NO. E-002/AI-94-378

ORDER APPROVING CONTRACT WITH
AFFILIATED INTEREST UNDER MINN.
STAT. § 216B.48

PROCEDURAL HISTORY

I. The Parties' Filings

On April 19, 1994 Northern States Power Company (NSP or the Company) filed a petition under the affiliated interest statute, Minn. Stat. § 216B.48, for approval of a 20-year contract to purchase 3.2 megawatts of baseload capacity and energy from an affiliated company, Minnesota Methane, LLC. The Company also requested contract approval under the cogeneration and small power production statute, Minn. Stat. § 216B.164.

On June 20, 1994 the Department of Public Service (the Department) filed comments asking the Commission to take the following action:

- (1) eliminate a contract provision allowing Minnesota Methane to increase contract capacity by 1.6 megawatts at contract prices until June 1, 1996;
- (2) eliminate a contract provision allowing Minnesota Methane to reopen price negotiations, should the Commission rule before April 30, 1996 that NSP's avoided cost for renewable resources is higher than the standard avoided cost on which contract prices were based;
- (3) approve the remainder of the contract;
- (4) grant the Company's request for an exemption from the statutory requirement (waivable by the Commission) to document its affiliate's cost of performance under the contract.

The Department made no recommendation on the Company's request for contract approval under the cogeneration and small power production statute.

On July 11, 1994 the Company filed reply comments opposing the contract modifications recommended by the Department. The Department and the Company later concurred in a staff recommendation to approve the two contract provisions the Department had challenged, subject to the requirement that the Commission review and approve those provisions if and when the

parties proposed to put them into effect.

The matter came before the Commission on January 12, 1995.

FINDINGS AND CONCLUSIONS

II. Summary of Commission Action

The Commission will approve the contract under the affiliated interest statute, conditioning approval of the contract terms challenged by the Department upon their review and approval at such time as the parties propose to put them into effect.

The Commission will require the Company to file the cost information required under the affiliated interest statute.

The Commission will take no action under the cogeneration and small power production statute, which does not require Commission approval of contracts successfully negotiated between utilities and qualifying facilities. The Commission will clarify that today's decision does not establish an avoided cost for renewable energy under that statute.

These actions will be explained in turn.

III. Commission Action Under the Affiliated Interest Statute

A. Statutory Background

Transactions between public utilities and affiliated interests are governed by Minn. Stat. § 216B.48 and Minn. Rules, part 7825.2200 B. All such transactions, with the exception of those involving amounts under \$50,000 or 5% of the utility's capital equity, require Commission approval. The burden of proof is on the utility to establish that the contract is reasonable and consistent with the public interest.

Contracts between utilities and their affiliates are not effective or valid until the Commission approves them. The Commission has continuing supervisory control over the contracts' terms and may disallow rate recovery of their costs if actual experience shows that contract payments were or are unreasonable.

A petition for approval must normally include documentation of the cost of providing the goods or services which are the subject of the contract. It must also include a copy of the proposed contract, a list and narrative description of all outstanding contracts between the utility and the affiliated interest, an explanation of why the contract is in the public interest, a description of any competitive bidding process used in awarding the contract, and an explanation of any decision not to use competitive bidding.

B. Contract Approval

The purchased power contract at issue is basically indistinguishable from the Company's purchased power contracts with non-affiliates. Its non-price terms properly reflect the importance of reliable supply and include penalty provisions designed to maximize reliability.

Its price terms are consistent with avoided cost¹ prices paid to other qualifying facilities and result in reasonably priced electric supply.

The two contract provisions initially challenged by the Department, Minnesota Methane's limited rights to add capacity at the contract price and to reopen price negotiations if the Commission establishes a special avoided cost for renewable energy, are potentially troublesome. The Commission agrees with the parties that the best way to deal with these provisions is to allow them to remain in the contract, subject to review and approval before they become effective. This will avoid premature decisionmaking and preserve the issues for informed decisionmaking if and when they arise.

The Commission concludes the contract is reasonable, consistent with the public interest, and should be approved.

C. Cost Data Required

The Company did not submit documentation of the costs Minnesota Methane will incur to provide service under the contract. The affiliated interest statute requires such documentation, unless the Commission finds its unnecessary:

. . . . No contract or arrangement may receive the commission's approval unless satisfactory proof is submitted to the commission of the cost to the affiliated interest of rendering the services or of furnishing the property or service to each public utility. Proof is satisfactory only if it includes the original or verified copies of the relevant cost records and other relevant accounts of the affiliated interest, or an abstract or summary as the commission may deem adequate, properly identified and duly authenticated, provided, however, that the commission may, where reasonable, approve or disapprove the contracts or arrangements without the submission of cost records or accounts. . . .

Minn. Stat. § 216B.48, subd. 3.

The Department and the Company believed cost documentation was unnecessary because the contract price, which is set by statute for qualifying facilities such as Minnesota Methane, does not depend upon the affiliate's costs. The Commission disagrees.

The statute requires that cost data be filed to protect the public from self-dealing in any form -- the artificially high prices that accompany windfall profits, the artificially low prices that accompany predatory pricing, and cross-subsidization of any kind. While using avoided cost to set price may adequately allay windfall profit concerns, it does not address other concerns underlying the filing requirement.

The Commission will therefore require the Company to file the cost data required under the affiliated interest statute.

¹ The federal Public Utilities Regulatory Policies Act of 1978, in an effort to introduce competition in electric generation, requires electric utilities to buy power produced by qualifying independent power producers and cogenerators ("qualifying facilities") at the cost of the utility's least expensive alternative source of new supply. This cost is the utility's "avoided cost."

IV. No Action under Cogeneration and Small Power Production Statute

The Company also requested contract approval under the cogeneration and small power production statute, Minn. Stat. § 216B.164. That statute authorizes the Commission to resolve disputes between electric utilities and qualifying facilities; it does not require Commission action on contracts successfully negotiated between those parties. Commission action on this contract would not be required if it were not with an affiliated interest.

Furthermore, since payments under contracts with affiliates are excludable from rate recovery until the utility has established their reasonableness in a general rate proceeding,² it is unclear what contract approval under the cogeneration and small power production statute would mean. For all these reasons, the Commission declines to act on the contract under the cogeneration and small power production statute.

Finally, the Commission clarifies that today's decision does not address the issue of the Company's avoided cost for renewable energy. Neither does it establish the prices in this contract as the Company's avoided cost for renewable energy. Those issues would require full evidentiary development lacking here.

ORDER

1. The contract between Northern States Power Company and Minnesota Methane is approved under Minn. Stat. § 216B.48, subject to the condition that the provisions on capacity additions and reopening price negotiations will be effective only upon Commission review and approval at such time as the parties propose to put them into effect.
2. Within 30 days of the date of this Order the Company shall file the information on Minnesota Methane's cost of providing service under the contract as required under Minn. Stat. § 216B.48, subd. 3.
3. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)

² Minn. Stat. § 216B.48, subd. 5.